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INTERCITY PASSENGER RAIL

Decisions on the Future of Amtrak and Intercity Passenger Rail Are Approaching

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Mr. Chairman and Members of the Committee:

We appreciate the opportunity to testify today on the National Railroad Passenger Corporation's (Amtrak) progress toward achieving operating self-sufficiency; its capital investment needs and how these capital needs compare with expected federal funding; and the future of Amtrak and intercity passenger rail. The Congress has directed Amtrak to be free of federal operating subsidies by the end of fiscal year 2002. This deadline presents serious implications for the future of Amtrak and intercity passenger rail service in this country. This statement is based on our recent reports on Amtrak financial issues.¹

In summary:

- Amtrak continues to struggle financially and must overcome substantial hurdles to reach operational self-sufficiency. Amtrak has made limited progress in reducing its budget gap—the gap that Amtrak needs to close to reach operational self-sufficiency. From fiscal years 1995 through 1999, Amtrak was able to reduce its budget gap by only \$78 million—from about \$554 million to \$476 million. From fiscal years 2000 through 2002, Amtrak will need to achieve about \$287 million in additional savings to reach operational self-sufficiency. Yet Amtrak has made limited progress toward this goal in the first 9 months of this fiscal year. Furthermore, Amtrak's costs are expected to increase, and Amtrak has a mixed record in controlling cost growth. In addition, Amtrak's ability to realize substantial revenue increases and productivity improvements is uncertain. Nearly three-quarters of the \$1.9 billion in net financial benefits that Amtrak expects to achieve between now and 2004 have either not been identified or are based on initiatives that have yet to be fully implemented.
- Amtrak has substantial short- and long-term capital investment needs that will be difficult to meet. From discussions with Amtrak managers and a review of published reports, we estimate Amtrak's identified capital needs to be at least \$9 billion through 2015 (in 1999 dollars). In addition, Amtrak will have other capital needs, such as acquiring new equipment, for which the company has not yet developed cost

¹*Intercity Passenger Rail: Amtrak Will Continue to Have Difficulty Controlling Its Costs and Meeting Capital Needs* (GAO/RCED-00-138, May 31, 2000), *Intercity Passenger Rail: Amtrak Needs to Improve Its Accountability for Taxpayer Relief Act Funds* (GAO/RCED/AIMD-00-78, Feb. 29, 2000), and *Intercity*

estimates. Amtrak will find it difficult to pay for these needs. Over the 2001 through 2004 period, the identified capital investment needs will exceed expected federal capital funds by nearly \$2 billion. Although some of this amount may be paid by other railroads that use Amtrak facilities, the federal government could be called upon to cover any funding shortfall, with capital financial support requested substantially higher than current levels.

- Key decisions will soon have to be made regarding the future of Amtrak, the nation's intercity passenger rail operator. If Amtrak does not reach operational self-sufficiency within the next 2 years, federal law requires that the Amtrak Reform Council submit a plan to the Congress for a restructured intercity passenger rail system and that Amtrak prepare a plan for its own liquidation.² On the other hand, if Amtrak does attain operational self-sufficiency, it could require a substantially higher level of financial support than it receives now to meet its capital needs and for certain railroad retirement expenses. In either case, the future of Amtrak will need to be decided. If that future does not include Amtrak, basic decisions must be made about an intercity passenger rail system. The decisions include the scope of a national intercity passenger rail network, if any; how it would be operated; and the level of federal funding that would be provided to support this network.

Background

The Rail Passenger Service Act of 1970 created Amtrak to provide intercity passenger rail service. Like other major national intercity passenger rail systems in the world, Amtrak has received substantial government support—over \$23 billion through fiscal year 2000. However, the Amtrak Reform and Accountability Act of 1997 (Amtrak Reform Act) prohibited Amtrak from using federal funds for operating expenses, except for an amount equal to excess Railroad Retirement Tax Act payments, after 2002.³ To help accomplish this goal, the Amtrak Reform Act provided Amtrak with flexibility to address certain costs. The act eliminated a statutory ban on contracting out work that would result in

Passenger Rail: Amtrak Faces Challenges in Improving Its Financial Condition (GAO/T-RCED-00-30, Oct. 28, 1999).

²The Amtrak Reform Council is an independent oversight body created by the Amtrak Reform and Accountability Act of 1997.

³Amtrak participates in the railroad retirement system, under which each participating railroad pays a portion of the total retirement and benefit costs for employees of the industry.

employee layoffs and abolished statutorily required labor protection arrangements that provided up to 6 years of compensation for employees who lost their job because of the discontinuance of intercity passenger rail service on a route or certain other actions. The Amtrak Reform Act required negotiations with the unions over new protection arrangements. To help achieve its financial goals, Amtrak has developed a series of strategic business plans.

Amtrak, like other railroads, is a very capital-intensive business. Since its creation, Amtrak has spent about \$10.2 billion in federal support for capital improvements and equipment overhauls. This amount includes about \$1.8 billion of the \$2.2 billion that Amtrak received through the Taxpayer Relief Act of 1997. These funds could be used for broadly defined expenses, including (1) acquiring equipment, rolling stock (such as passenger cars and locomotives), and other capital improvements; (2) upgrading maintenance facilities; (3) maintaining existing equipment in intercity passenger rail service; and (4) paying of interest and principal on obligations incurred for these purposes. Amtrak has also obtained capital funding from state and local governments, generally for specific capital investments, and from the commercial debt markets. These funds support Amtrak's 22,000-route-mile passenger rail system, including 650 miles of track owned by Amtrak. Amtrak maintains an active fleet of 2,600 cars and locomotives.

Amtrak Will Have to Overcome Major Hurdles to Become Operationally Self-Sufficient

Amtrak continues to struggle in its quest to become operationally self-sufficient by the end of 2002. Amtrak has made relatively little progress over the past 5 years, and the results for the first 9 months of the current fiscal year in reducing its budget are not encouraging. This means that substantial additional progress will be required over the next 2 years to attain operational self-sufficiency. One of Amtrak's difficulties in reaching operational self-sufficiency is controlling its costs, particularly labor costs. Finally, Amtrak has yet to fully implement the various revenue enhancing and productivity improvement initiatives that it considers important to operational self-sufficiency, including its Acela Express service.⁴

⁴Acela Express is part of Amtrak's high-speed rail program on the Northeast Corridor. Acela Express trains are expected to reach speeds of up to 150 miles per hour and have trip times of about 3 hours between New York City and Boston and about 2-1/2 hours between New York City and Washington, D.C.

Most Financial Results Needed to Reach Operational Self-Sufficiency Are in the Future

Amtrak has made limited progress in moving toward operational self-sufficiency in the last 5 years. According to Amtrak, its budget gap⁵ fell by \$78 million during fiscal year 1995 and through 1999—from about \$554 million in fiscal year 1995 to \$476 million in fiscal year 1999.⁶

Through the first 9 months of the current fiscal year (October-June), Amtrak's revenue increased by 11 percent over the same period in 1999. But, expenses increased by 7 percent. Since Amtrak has about \$3 in expenses for every \$2 in revenue, the increase in expenses for the most part negated revenue gains. As a result, the budget gap was only about \$33 million lower than it was for the same period in 1999. Amtrak officials agreed that additional actions are needed during the final 3 months of this year to achieve the planned budget gap reduction of \$114 million and that achieving its goal will be difficult. Amtrak attributes the problems to the delayed rollout of the Acela Express service and a slower-than-expected increase in its mail and express business.⁷

The limited progress that Amtrak has achieved in reducing its budget gap makes it essential that Amtrak make substantial strides over the next 2 years to achieve operational self-sufficiency. To become operationally self-sufficient by 2002—that is, to reduce its budget gap to no more than the amount of excess Railroad Retirement Tax Act payments—Amtrak will have to reduce its budget gap by an additional \$287 million⁸ over what it was in fiscal year 1999. This is nearly four times the reduction that Amtrak made in the last 5 years. It is therefore critical that Amtrak take those actions necessary to control cost growth and achieve the revenue projections contained in its latest business plan.⁹

⁵Amtrak defines budget gap as the corporation's net loss (total revenues less total expenses) less capital-related expenses, including the depreciation of its physical plant, other noncash expenses, and expenses from its program to progressively overhaul railcars (i.e., to conduct limited overhauls of cars each year rather than comprehensive overhauls every several years).

⁶The 1998 budget gap excludes \$36 million in retroactive payments under recently negotiated labor agreements.

⁷"Express" is the transportation of higher value, time-sensitive goods, such as produce.

⁸This amount represents the \$476 million budget gap in 1999 less expected excess Railroad Retirement Tax Act payments in 2002 of \$189 million.

⁹In addition, Amtrak's overall financial condition has also not improved. Through the first 9 months of this year, Amtrak's net loss was about \$711 million—about \$6 million higher than it was for the same period in fiscal year 1999 (\$705 million). Amtrak's lower-than-expected performance appears to be related to higher expenses rather than lower revenue.

Amtrak Will Continue to Have Difficulty Controlling Its Costs

Amtrak has had and will continue to have difficulty controlling cost growth. Amtrak met its expense targets in 1998 and 1999 but missed them from 1995 to 1997 and, overall, its expenses have been about \$150 million more than planned over this period. Amtrak's strategic business plans have generally tried to hold cost increases to no more than the rate of inflation. But, as we recently reported, Amtrak's operating costs increased by about 12 percent over the rate of inflation from 1995 through 1999.¹⁰ Amtrak's inflation-adjusted costs (1999 dollars) were about \$2.4 billion in 1995 and about \$2.7 billion in 1999. Amtrak has attributed increased costs to, among other things, the results of labor negotiations, expanded service levels, increased depreciation, and the implementation of its progressive overhaul program. While Amtrak has "spent money to make money," it has realized little benefit from the expenditures it has made. For example, in 1995, for every operating dollar that Amtrak spent, it earned \$0.65 in total revenue. In comparison, Amtrak earned \$0.67 in total revenue for every dollar spent in 1999. Through the first 9 months of this fiscal year, Amtrak has earned about \$0.64 in total revenue for every dollar expended.

Labor costs represent Amtrak's single largest operating cost—about 52 percent of total operating costs in 1999. Amtrak's labor costs have increased since 1995—about 10 percent above the rate of inflation (from about \$1.3 billion to about \$1.4 billion). This is a net increase, that is, net of the savings achieved through such actions as negotiated productivity improvements. In part, this increase reflects the fact that the size of Amtrak's workforce has not changed materially in recent years. In 1999, Amtrak employed about 22,500 agreement (union represented) employees and about 2,700 management employees—about the same total as in 1994 when Amtrak started to reduce its workforce. Amtrak officials attributed employment increases to such things as service expansion and capital investments. In part, increases in labor costs may also reflect that Amtrak has no standard measures of labor productivity for its different lines of business (e.g., intercity passenger rail service and commuter service). Such measures would allow Amtrak to determine its efficiency and better manage cost growth.

¹⁰See GAO/RCED-00-138.

Amtrak's cost growth can be expected to continue. Amtrak's operating plan for 2000 shows that overall operating costs will increase by a net \$60 million over the next 5 years.¹¹ This is a net increase because it includes growth in such costs as labor and interest expenses as well as savings from such things as productivity improvements. Regarding labor costs, Amtrak has entered into a new round of collective bargaining with its union-represented employees. If the new round of bargaining follows the pattern of past negotiations, substantial cost increases can be expected. As a result of collective bargaining for 1998 to 1994, Amtrak estimated that wages increased between \$120 million and \$140 million. As a result of the most recently completed round of bargaining (1995 to early 2000), Amtrak estimated that wage payments increased by \$144 million through 1999.¹²

Important Business Plan Initiatives to Increase Revenues and Improve Productivity Have Yet to Be Fully Implemented

Amtrak's plans to reach operational self-sufficiency emphasize business growth, particularly increasing revenues and improving productivity. Over the next several years, Amtrak expects substantial increases in revenue from such initiatives as implementing its Network Growth Strategy (a strategy to increase passenger and mail and express business) and new service standards designed to ensure a consistent, high-quality product. Amtrak's most recent business plan update estimates that initiatives such as these will result in net financial improvements of about \$1.9 billion through 2004.

Nearly three-quarters (\$1.4 billion) of the net financial benefits that Amtrak expects to achieve from 2000 through 2004 have either not been identified or are based on initiatives that Amtrak has not yet fully implemented. (See table 1.) These include such initiatives as expanding the mail and express program, developing actions to improve productivity, implementing the market-based route network, and implementing service standards. Amtrak officials told us they are in the process of defining the specific actions associated with these initiatives but agreed they had not yet been fully defined. That Amtrak has not

¹¹This includes the costs of progressive overhauls. Amtrak funds progressive overhauls through its capital program. However, under generally accepted accounting principles, the cost of such overhauls are considered an operating expense.

¹²Total negotiated wage payments (including general wage increases, signing bonuses, and retroactive payments) were \$260 million. Amtrak expects to pay the balance of this amount (\$116 million) in 2000.

fully implemented its most important business plan initiatives increases the uncertainty about whether it can meet its financial goals over the next 2 years.

Table 1: Estimated Financial Impacts of Amtrak's Business Plan Initiatives, Fiscal Years 2000 Through 2004

Dollars in millions

<u>Initiative</u>	<u>Change in revenues</u>	<u>Change in expenses</u>	<u>Net impact</u>
Productivity actions to be determined	\$70.3	-\$803.6	\$874.0
Aligning route structure to customer demand	30.0	-205.0	235.0
Increasing ticket revenue	175.2	5.9	169.2
Mail and express expansion	274.3	181.4	92.9
Productivity actions to offset inflation ^a	0	-54.2	54.2
Subtotal	\$549.8	-\$875.5	\$1,425.3
Implement other initiatives	429.5	-80.7	510.2
Total	\$979.2	-\$956.2	\$1,935.5

Note: Totals may not add due to rounding. Amtrak's business plan does not contain a separate initiative for its Acela Express service. Rather, Acela Express is integrated into the plan as a whole.

^aAmtrak officials told us that this initiative is a combination of actions designed to achieve cost savings to offset potential cost increases due to inflation. These activities include wage and work rule changes, revenue enhancements, and improved food and beverage management.

Source: GAO's analysis of Amtrak's data.

In addition, Amtrak has encountered difficulties in implementing high-speed rail service on the Northeast Corridor. Amtrak's Acela program is one of the cornerstones of Amtrak's plans to eliminate the need for federal operating subsidies. In January 2000, Amtrak began Acela Regional service on a limited basis between Washington, D.C., and Boston.¹³ However, the introduction of Acela Express has been delayed by mechanical problems since September 1999, and Amtrak has yet to announce a start date for this service. Amtrak expected the Acela Express to generate about \$180 million in net revenues by 2003. Amtrak officials agreed that revenues have been lost because of Acela Express delays and are still quantifying these losses as the delay continues. According to Amtrak, the company is currently identifying actions that might be needed to offset lost Acela Express revenues and reduce Amtrak's budget gap as a whole. The loss of Acela

¹³Acela Regional is designed to replace Amtrak's current NortheastDirect, Empire, and Keystone service and will offer improved equipment, trip times, and schedules.

Express revenue increases the pressure on Amtrak to make even more progress in other areas over the next 2 years to reach operational self-sufficiency.

Amtrak's Capital Needs Could Require an Increase in Federal Support

Amtrak has substantial capital investment needs that could result in requests for increases in federal capital support. As we recently reported, these needs total over \$9 billion through 2015.¹⁴ These needs include making safety improvements on the Northeast Corridor, bringing the Northeast Corridor up to a condition where only routine maintenance is required (called “state of good repair”), and overhauling equipment. However, Amtrak will have difficulty funding these investments. We estimate that Amtrak’s capital investment needs will exceed expected federal funding by nearly \$2 billion from 2001 through 2004. The shortfall will likely be higher since it does not include capital investment needs for which Amtrak has not developed cost estimates.

Amtrak Has Significant Short- and Long-Term Capital Investment Needs

Amtrak has significant capital needs, both in the short-term (2001 through 2004) and in the long-term (2005 through 2015). Our discussions with Amtrak officials and review of reports show Amtrak’s capital investment requirements over the next 4 years (through 2004) to total at least \$4 billion. Infrastructure investment needs account for over \$2.5 billion of the total and are targeted toward addressing deferred maintenance and improving the quality of service on the Northeast Corridor.¹⁵ Included in these investment needs is about \$316 million to continue safety investments at various locations on the Corridor. According to an Amtrak analysis, these investments are primarily concentrated on the tunnels leading into and out of New York City’s Pennsylvania Station—a station that serves over 300,000 intercity and commuter rail passengers daily. In addition, about \$1.2 billion will be needed to eliminate deferred maintenance and restore the Corridor’s infrastructure to a condition where only routine maintenance is required. Other short-term capital investment needs include reducing equipment maintenance backlogs in the

¹⁴See GAO/RCED-00-138. All amounts in this section are in constant 1999 dollars. Amtrak has not comprehensively identified its short- and long-term capital investment needs. Therefore, to identify these needs, we asked Amtrak managers to identify capital investments they believed are needed to maintain current service levels and improve Amtrak’s service and reviewed Amtrak and other reports addressing capital investment needs. As a result, the needs we identified may not be the same as those that might have been identified by Amtrak, had it comprehensively identified its capital needs.

¹⁵Amtrak expects to share some portion of this cost with other users of the Northeast Corridor.

progressive overhaul program (at an estimated cost of over \$1 billion), repaying debt principal for the acquisition of cars and locomotives (\$346 million), and upgrading maintenance facilities (\$42 million).

Amtrak's long-term capital investment needs also focus heavily on the Northeast Corridor. We estimate that at least \$5.1 billion in investments may be needed from 2005 to 2015. These capital investment requirements include making further safety improvements to tunnels, including those leading into and out of Pennsylvania Station, continuing to restore the Corridor to a state of good repair, and completing the high-speed rail program. Most of the long-term capital investments we identified (about \$4.5 billion) are concentrated on continuing the restoration of the Northeast Corridor's infrastructure to a state of good repair. Other long-term capital investment needs include replacing bridges and tunnels on the Northeast Corridor and replacing and rehabilitating the Corridor's electric power system (a system that supplies power to Amtrak's trains and dates from the 1920s to the 1940s). These investments would replace aging systems that are prone to mechanical failures and allow for growth.

In addition to the identified short- and long-term capital needs, Amtrak will have other capital investment needs for which it has not developed cost estimates. These include equipment maintenance needs and new capital investment needs, such as station renovations and acquiring new equipment. Although Amtrak acquired a large number of passenger cars and locomotives during the 1990s, some components of Amtrak's fleet are past their useful lives and will need to be replaced. Finally, Amtrak will have capital investment needs related to implementing its Network Growth Strategy, expanding its express program, and developing new "high-speed" rail corridors across the country.

Potential Funding Shortfalls May Require Additional Federal Support

Amtrak's identified capital investments will exceed expected levels of federal capital funds by nearly \$2 billion over the 2001 through 2004 period. Since Amtrak has never covered the cost of its operations, it has relied solely on external funds for capital investments. This has included the federal government, state and local governments, and the commercial debt market.

Amtrak should be able to meet its planned investment requirements through 2000 from Taxpayer Relief Act funds and the fiscal year 2000 federal capital grant. However, beginning in 2001, Amtrak's capital investment requirements will exceed expected available federal funding. The shortfall assumes that Amtrak will receive federal capital grants of \$521 million annually through 2004.¹⁶ In reality, Amtrak's funding shortfall will be more than \$2 billion because our analysis does not include investment requirements for which Amtrak has not yet developed cost estimates. The potential shortfall in federal capital funds will require Amtrak to rely heavily on sources other than federal capital grants to meet some its needs. However, the federal government may well be called upon to fund these shortfalls in amounts substantially higher than current funding levels.

Analyzing Amtrak's capital needs and expected funding to meet these needs is made more difficult because Amtrak has not prepared a multiyear capital plan since 1997. Instead, it has developed a series of capital plans that cover only a limited horizon—not more than 1 year at a time. These plans do not fully describe Amtrak's current and future capital investment requirements and how they will be funded, or indicate their relative priority. Amtrak has stated that it expects to issue a multiyear capital plan later this year.

Time Nears for Decisions on the Future of Amtrak and Intercity Passenger Rail

Amtrak is under extreme pressure to reach operational self-sufficiency by the end of 2002. In our opinion, no matter whether Amtrak succeeds or fails in this endeavor, important decisions will need to be made about the scope of intercity passenger rail service and the level of federal support, if any.

If Amtrak attains operational self-sufficiency, it will likely need substantially more funds than it currently receives. As discussed earlier, we estimate that Amtrak will need at least \$9 billion to meet its identified capital needs through 2015. This amount does not include needs for which cost estimates have not been made. In addition, Amtrak will require substantial funds annually to cover excess Railroad Retirement Tax Act payments, an

¹⁶Our analysis is based on Amtrak receiving \$521 million in capital grants beginning in 2001. Amtrak's most recent business plan update also assumes that Amtrak will receive this level of capital funding through 2003. No estimate was available for 2004. Recently introduced bills, if enacted, could provide capital funds for Amtrak. S.1900 and H.R. 3700 allow Amtrak to issue \$10 billion in bonds over 10 years for capital improvements to Amtrak's Northeast Corridor and other high-speed rail corridors.

operating expense for which it may receive federal funds under the Amtrak Reform Act (e.g., according to Amtrak, \$190 million in 2003 and \$200 million in 2004). The federal government could be called upon to provide support for both Amtrak's capital needs and excess Railroad Retirement Tax Act payments, which could total more than the \$521 million that Amtrak currently receives in federal support.

On the other hand, if Amtrak fails to reach operational self-sufficiency, the Amtrak Reform Act requires that the railroad submit to the Congress a liquidation plan, and the Amtrak Reform Council submit a plan to the Congress for a restructured national intercity passenger rail system. As a result of any congressional action on these plans, the nation's intercity passenger rail service could have a considerably different look.

In either situation, the future of Amtrak, and, by extension, the future of intercity passenger rail in the United States need to be decided. Given that 2002 is just 2 years away, it is not too early to begin considering a long-term vision for Amtrak and intercity passenger rail and how this vision should be structured. If that future does not include Amtrak, basic decisions about an intercity passenger rail system need to be made. This would include determining the scope of an intercity passenger rail network, if any; how it would be operated; and what level of funding would be provided to support this network.

Mr. Chairman, this concludes our testimony. We would be pleased to answer any questions you or Members of the Committee may have.

Contact and Acknowledgements

For information regarding this testimony, please contact Phyllis F. Scheinberg at (202) 512-3650. Individuals making key contributions to this testimony were Helen Desaulniers, Richard Jorgenson, and James Ratzenberger.

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